LDTI: a comprehensive view of implementation at US life insurers

November 2021

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Foreword

Last year, the Financial Accounting Standards Board (FASB) voted to delay the effective date of the US Targeted Improvements to the Accounting for Long-Duration Contracts (LDTI) accounting rule for the second time, to 1 January 2023 for public entities (SEC filers) and to 1 January 2025 for other entities.

FASB did this to help alleviate the impact of Covid-19 and allow insurers the best chance of meeting the LDTI deadline, but firms continue to face challenges with implementation of the standard.

Issues around interpretation, communication, systems and data requirements have complicated the move, particularly for insurers who are less resourced than others.

To help understand the challenges US life insurers face in implementing LDTI, *InsuranceERM* spoke to five firms – National Western Life Insurance, Global Atlantic, Cigna, Unum Group and Pacific Life – to gain insights into the process.

In this report, sponsored by Moody's Analytics, we look at the implementation status and the obstacles firms might face as they move towards the LDTI deadline, including specific issues around volatility, communication and finance system modernisation.

Actuaries and consultants play a crucial part in insurers' implementation projects and we have sought views from the Society of Actuaries and Valani Global.

We thank all the participants for their insightful comments. ■

Cintia Cheong,
Senior Staff Writer,
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The report gathers thoughts and views from a cross section of the industry. The feedback gathered tells us most are on target for implementation in 2023. They plan to finish implementation by end of 2021 with the intent to run parallel for three to four quarters in 2022. Some participants also suggested that they plan to use time in 2022 to review additional disclosure and reporting requirements including the need for detailed attribution analysis.

Across the group, participants identified a number of challenges in their LDTI implementation including:

- Data management: data sourcing, storage, and infrastructure
- Actuarial and financial transformation initiatives running in parallel
- Coordination across the streams
- Interpretations of the standard and adapting policy changes. For instance, LDTI's impact on reinsurance, especially in situations where the reinsurer provides administrative accounting and actuarial services
- Aligning LDTI project goals with these broader initiatives
- Resource constraints
- Increased volatility of financials

A significant revamp of data is required for actuarial and accounting processes, to capture and understand the changes from LDTI. Preparation of data is critical, including calculating data at policy cohort levels.

Responses also tell us that insurers are still evaluating the anticipated balance sheet volatility from LDTI. They do expect additional volatility in GAAP earnings driven by market risk benefits as well as interest rates. More importantly, they expect additional challenges in being able to adequately explain the drivers of volatility.

In addition, some insurers view LDTI as an opportunity to modernise. Many are taking a strategic approach and using LDTI as an impetus for modernisation. This creates the need for more process and analyses that requires interpreting and communicating financial results over short periods of time for long duration products. It is inherently complicated and communicating the impacts is key to successful implementation.

In summary, this report provides a comprehensive view on the current state of LDTI implementation, industry preparedness and additional challenges that need to be addressed. We hope you find this report valuable. We thank all the participants for their insights. ■

Srini Iyer,
Senior Director,
Moody's Analytics

Insurers' views on LDTI

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Paul Lavallee, Corporate Actuary, Unum Group
Adam Lei, Head of Enterprise Risk Management at National Western Life Insurance
Sarah Williams, Deputy Chief Risk Officer, Global Atlantic Financial Group
Jill Chen, Director and Actuary, Pacific Life
Mary Terese Agoglia Hoeltzel, Global Chief Accounting Officer, Cigna

What is the current status of your LDTI implementation and does the effective date of 2023 give you enough time?

Sarah Williams: We are working towards implementation of LDTI with plans to adopt on 1 January 2023. Our teams have been on this journey for three years now and although the timing is challenging, we have implemented a robust project management effort with strategic use of contractors/consultants to meet the public company deadline.

Paul Lavallee: We formally started our implementation project three years ago when the standard was released. I'd say we are well positioned within the timeline. We've got the base models done, now we're gearing up for parallel runs. Looking ahead, we are planning to build LDTI into our financial projection models, and into our valuation and accounting close processes, including building out all the controls and all the ancillary tools that we have around these.

At this point we're comfortable with where we are heading to 2023 when we go live. The deferrals of the implementation date from FASB were welcome in both instances. The original date would have been a real stretch for us and for the rest of the industry.

Mary Hoeltzel: We are tracking according to our project plan, which is designed to allow for testing and parallel runs in 2022, prior to our Q1 2023 effective date.

Adam Lei: We are in the middle of data infrastructure modernisation, actuarial model changes, and process redesign. We have yet to

Paul Lavallee, Unum Group

complete our first valuation run under LDTI.

To comply with LDTI, a more robust data infrastructure and higher quality data are required. One of the first steps in this "data journey" is to perform a deep cleanse of the existing data. From there, we build out the new data infrastructure, with the support of a new insurance administration system, to ensure data quality going into the new world of LDTI.

Regarding actuarial model changes and process redesign, the goal is to incorporate system features as developed by our vendors to meet the requirements of LDTI into the new reporting processes. Our current valuation models were not designed with "attribution analysis", etc., in mind. While we can perform high-level attribution, it is ad-hoc and general in nature, which can't satisfy the enhanced communication considerations under LDTI.

We plan to have the first valuation run by the end of 2021, then move into dual track reporting, reconciliation analysis, and attribution analysis during 2022. We are on track to achieve such goals.

Jill Chen: Since my company is a non-SEC filer (i.e. non-public company), we have until 2025 to adopt LDTI. Currently we are focusing on updating our actuarial modelling system to be in compliance with LDTI, at the same time as building our next generation data store and financial control process. In general, we feel confident about meeting the 2025 effective date timeline.

What is the biggest challenge you face with regards to LDTI?

Paul Lavallee: Some of the challenges have been related to some of the emerging interpretations of the standard. FASB and the Insurance Expert Panel have developed interpretations, and there have been some instances where we've had to adapt our accounting policies and modelling to these. It's been a little bit challenging, but overall, we feel good about where we're at now.

Jill Chen: The biggest challenge in our LDTI implementation journey thus far is to align LDTI project goals with these broader data and financial system modernisation initiatives, making sure workstreams are well coordinated in driving to our ultimate modernisation goal.

Mary Hoeltzel: Some of the challenges we have seen have been around data requirements and data infrastructure, changes to actuarial valuation platforms, and overall organisation and change management. Perhaps one of the greatest challenges looking back since the standard was published has been dealing

Adam Lei, National Western Life Insurance

with LDTI's impacts on reinsurance, especially in situations where the reinsurer provides administrative accounting and actuarial services.

There are certainly challenges with adopting LDTI related to data requirements and data infrastructure that require time and resources to address. Those challenges are not isolated to reinsurance, but reinsurance is of course a component of the data considerations.

Adam Lei: The biggest challenge has been resource constraints and attention/engagement from senior leaders and the Board.

Sarah Williams: In my view, the increased volatility of GAAP financials is going to be the biggest challenge for insurers. The new guidance is expected to increase financial statement volatility primarily due to the requirement to measure market risk benefits at fair value. The challenge lies in the differences between GAAP, statutory and economic models, and the conflicting incentives for US insurers to hedge under one regime versus the other.

How will your actuarial, accounting and analytics change under LDTI, and how will that impact your processes?

Sarah Williams: Our actuarial and accounting processes are being revamped to ensure that we are able to capture and understand the changes from LDTI so that we can clearly communicate them to management. We've been making changes to improve our models, data and reporting. We also are building enhancements to our risk models to better predict the LDTI changes under various scenarios.

Adam Lei: We added two new positions to the actuarial team focusing on LDTI implementation – their roles include data cleanse, collaboration with IT to build a more robust valuation infrastructure and working with system vendors to implement new system features required under LDTI. We also added a new position at Accounting/Finance, mainly in dual reporting (current GAAP and LDTI), reconciliation analysis, collaboration with our audit firm, enhancing communication processes, etc. IT has dedicated significant resources to the actuarial and accounting/finance departments.

We are currently in a process of redesign. LDTI comes with tremendous challenges not only to the foundational capabilities such as data and actuarial valuation, but also attribution analysis via source-of-earning analysis and reconciliation between the old and the new standards. Our current processes, including the quarterly close calendar, won't be adequate under the new standards. We are working with external consultants on process redesign.

Mary Hoeltzel: While we are still evaluating this, certain process changes will be necessary in response to new financial information as well as substantial additional disclosures, unlocking requirements and, in some cases, new or enhanced systems.

Paul Lavallee: One of the approaches that we took when we started implementing the standard was trying to harmonise our actuarial models, using LDTI as a catalyst for modernisation. A lot of our work over the past few years has been on interpretation of the standard, setting accounting policies, and then building our base models and our LDTI solutions around these requirements.

It's been a lot of work, a big investment in the project, but from our perspective it is paying off in terms of having a consistent LDTI input data format, actuarial calculation, and output. And we're seeing those benefits as we're moving to the next phases of the project, which are really around productionising, building the control environment, and building out the metrics and analytics that we'll need to support the reporting and stakeholder communication and education.

Sarah Williams, Global Atlantic Financial Group

What are the data challenges associated with LDTI? Are you able to get enough granular data to meet your requirements?

Mary Hoeltzel: We have not run into problems with data granularity.

Adam Lei: Yes, we are able to get sufficient data to support the modified retrospective approach.

Paul Lavallee: The actuarial reserve calculations are being done at a cohort level, introducing different levels of granularity to the results. In some respects, it's more aggregated than how we looked at our active life policy reserves today. That creates one challenge in terms of attributing the cohort reserves for analysis purposes.

But then when we think about data flowing downstream to the financial reporting, certainly there is a lot more information to be presented in terms of liability and data roll forwards, for example. So we are developing structures that require multiple reserve engine runs, for example, so the data feeds downstream to produce that level of information for financial reports.

Preparing the data is critical. One of the other challenges is taking granular cohort-level calculations, which produce a lot of information, and distilling to the key messages. I've received comments from people saying "Wow this is great. You can produce cohort-level reports for us to analyse every quarter". And I have to turn to people and ask them "do you really want to review 50 different reports for every segment?" No, I think you really need to distil the key messages but also summarise the key moving pieces. Those are some the challenges that we need to reckon with.

Sarah Williams: Fortunately, when we analysed the data requirements for our business, we did not identify significant data gaps in the feeds that we received.

LDTI is anticipated to introduce a lot of volatility on balance sheet. How concerning is this for you and is it something that you've communicated to market?

Adam Lei: We are well aware of the volatility on the balance sheet under LDTI, particularly for businesses under FAS 60. Fortunately for us, the majority of our business is in FAS 97, not FAS 60. As such, volatility of our balance sheet won't be materially different before and after. However, we are building analytics around the small blocks under FAS 60.

Sarah Williams: I expect the amount of GAAP volatility resulting from LDTI market risk benefits, particularly as it relates to interest rates, will be meaningful. Hedging the full sensitivity under LDTI could cause significant breakage with statutory capital models, and therefore may not be feasible for many insurers. It will be interesting to see how markets react to this over time and whether there will be pressure on insurers to modify their hedge programs in response. We have disclosed this expected volatility in our public filings.

Mary Hoeltzel: We are still evaluating the impact of adoption. While LDTI will be impactful for us, as a global health services organization with a wide variety of products, only a subset of Cigna's business is impacted by LDTI [such as] certain supplemental health, life and accident insurance products.

Paul Lavallee: It's still a daunting task to build the metrics and to think about educating all of our different stakeholders around what's going to be different in the LDTI world compared to current GAAP. Some aspects of the standard will introduce more volatility, such as regular assumption updates, and the requirement to remeasure AOCI [Accumulated Other Comprehensive Income] at the prescribed single A rate. Other aspects will tend to mute volatility, such as the interaction between claims experience and the net premium ratio

Jill Chen, Pacific Life

underlying policy reserves.

When we think about the communication, the challenges include explaining volatility but also more broadly educating our stakeholders to understand how the LDTI measures relate to the true underlying nature of the business. As we look out over the next year and a half to two years, there's definitely a lot of work ahead. The education component and building out the metrics are key next phases of the project for us.

To what degree are you using LDTI as a catalyst for finance system modernisation?

Mary Hoeltzel: To some degree. IFRS 17 necessitated certain data centralisation solutions, and with our implementation of LDTI we are leveraging and enhancing some of those solutions.

Paul Lavallee: We are using LDTI as an impetus for modernisation. LDTI is going to create a lot more processes and analyses that we'll have to do within the timeline for each financial close, so we need to build efficiency to handle the increased complexity. Because of the nature of the basis of LDTI - it's not locked in, we're on a best estimate basis - it's going to compel our actuarial and finance groups to really understand what's going on behind the business. This will definitely emphasise the need for good, nimble finance systems.

Jill Chen: LDTI not only introduces market risk benefit (MRB), but also brings new disclosure requirements including liability roll forwards and information about significant inputs, judgements and assumptions, which acted as one of the catalysts for us to modernise our actuarial modelling platform as well as, more broadly, our financial system architecture.

Adam Lei: We are a small company, with significant resource constraints. As such, we have to balance the considerations between compliance and as a catalyst for system modernisation.

We had performed a series of data cleaning activities, built out data infrastructure, and are in the middle of process redesign, to the extent to support LDTI.

Personally, and from my previous experience, I have seen LDTI being used as a rallying cry and strategic initiative at large insurance companies. One such company spent and plans to spend considerable resources, north of $50m to fundamentally reshape its data infrastructure, actuarial system, accounting system, and internal/external communication capabilities.

Sarah Williams: Early on, we made the decision to migrate our actuarial models to a new platform at the same time we started LDTI. This migration is enabling us to consolidate our models, streamline the data processing, and implement stronger model governance and controls. For us, it was not a choice but more like a requirement to be able to handle the actuarial reserving and financial reporting under the new standard and meet our public company reporting deadlines.

What are the challenges of interpreting results and communicating to the street?

Adam Lei: LDTI presents significant communication challenges, particularly for insurers with large FAS 60 books.

My personal observation is that book value equity at some insurance companies may decline dramatically, or even reverse from positive to negative. However, such changes may not be unique to individual companies but most likely an industry norm. As such, communications of LDTI results can be conducted within this industry context.

Nonetheless, a robust source of earning analysis and earnings attribution report will help external stakeholders better comprehend the results under LDTI, particularly so for the first few reporting cycles. Such strong analytical reports will not only deepen senior management's understanding of their businesses, but also help strengthen external stakeholders' confidence on managements' capabilities. My personal view is that communication challenges from LDTI can be used to strengthen, not weaken, external perception of the companies.

LDTI also provides opportunities for non-GAAP measurements such as embedded value, value of new business, economic capital, etc. Since market-to-book (MTB) ratios may be less relevant under LDTI, new economic measurements, which in many ways are far superior to the MTB ratios, can be developed along with LDTI and used in external communications.

Internally and particularly for public insurance companies, communications on LDTI results and the associated incentive programme changes will be critical to keep employee morale and productivity.

Sarah Williams: I expect that companies will need to be able to clearly explain the market sensitivities to the street, particularly those that do not hedge, and whether they view those sensitivities as economic or not. This puts increased pressure on insurers to ensure that they have strong internal economic models to guide risk management decisions.

Paul Lavalle: Communicating the impacts is key. It's an accounting standard, it doesn't change the underlying economics of the business. It doesn't change the view of our value proposition and how we look at the enterprise. But it is one of the challenges to make sure that our stakeholders understand what's changing with the standard and what the new metrics represent.

For both internal and external stakeholders, the challenge is for them to understand some of the dynamics around OCI [other comprehensive income] adjustments and the beginning balance. And then there'll be multiple layers of changes that we will see coming through earnings.

Mary Terese Agoglia Hoeltzel, Cigna

There will be changes from the transition for companies that are using the modified retrospective approach, and other differences from current GAAP are based on the valuation principles at play for both liabilities and for DAC [deferred acquisition cost]. For companies with market risk benefits, that of course is a whole different topic as well. There is a broad range of challenges that we and the industry as a whole are working to address.

Mary Hoeltzel: As a global health services organisation with a wide variety of products, only a subset of Cigna's businesses is impacted by LDTI. This standard highlights the importance of having a strong cross-functional team, with actuaries and accountants collaborating to communicate effectively across the organisation. The accounting and disclosures required by LDTI are highly dependent on the actuarial processes and data produced by the actuaries and actuarial valuation systems, so we each have to step outside of the comfort zone of our own functional area.

Which of the following are critical in your design of an LDTI subledger solution? Select all that apply:

- **Sub-cohort / seriatim level reporting**
- **Support for multi-currency and interim reporting**
- **Ability to produce STAT reporting (VM-20, VM-21, VM-31) from the same solution**
- **Ability to produce delta GL entries between STAT and GAAP**

Paul Lavallee: These are all important.

Sarah Williams: Sub-cohort / seriatim level reporting and the ability to produce stat reporting (VM-20, VM-21, VM-31) from the same solution.

Jill Chen: I'd pick the last two options as critical in designing LDTI subledger.

Mary Hoeltzel: We are not implementing a subledger solution. That said, in other aspects of our LDTI build, "support for multi-currency and interim reporting" is critical to our design.

Adam Lei: Sub-cohort / seriatim level reporting is important to us. A significant amount of our resources, both actuarial and IT, was spent on getting this in place.

Ability to produce delta GL entries between STAT and GAAP will be important in the next phase, i.e. reconciliation and attribution analysis. ■

The actuarial perspective

Tara Wolf and Michael Hughes explain the difficulties actuaries face with LDTI.

Contributors:
Tara Wolf, Fellow of the Society of Actuaries
Michael Hughes, Fellow of the Society of Actuaries

In general, what is the current status of LDTI implementation for actuaries and does the effective date of 2023 (or 2025) give them enough time?

Tara Wolf: The current status varies widely across the industry. Many public companies are in the process of dry runs for the new valuation/reporting processes and getting comfortable describing what the results mean, while others are still developing their capabilities and will have a flurry of activity as they work to get ready for the effective date. I expect the public companies will all get there, but it will be a bit more of a sprint for some of them than others. Naturally, some of the non-public companies are not as far along but they should have adequate time provided they mobilise soon.

What is the biggest challenge actuaries face with regards to LDTI?

Michael Hughes: One of the biggest challenges has been the need for strong cross-functional collaboration and teaming across the organisation (between actuarial, finance, accounting, information technology as well as across business units) due to the interdependencies and complexities of the new standard. LDTI and related modernisation objectives have necessitated a stronger partnership between actuarial and IT. Resources are also in short supply, as there are many competing priorities and demands on actuaries' time.

How will insurers' actuarial, accounting and analytics change under LDTI, and how will that impact their processes?

Tara Wolf, Fellow of the Society of Actuaries

Michael Hughes, Fellow of the Society of Actuaries

Michael Hughes: Many of the management reports and analytics currently used will change going forward. LDTI provides an opportunity for valuation actuaries and their customers to rethink and redefine the high quality report set needed going forward to control, analyse and explain results.

The new reserve and DAC [deferred acquisition costs] roll forward disclosures will help with this. From a broader management reporting standpoint, the changes to analytics and key performance indicators – and the linkages to economic value - will vary by product line and reflect changes in the sources of earnings, earnings patterns and drivers of earnings and balance sheet volatility. Most companies will likely make some updates to their non-GAAP measures as a result. More work is needed at most companies to enhance management reporting and associated planning and forecasting capabilities under LDTI.

What are the data challenges associated with LDTI – are actuaries able to get enough granular data to meet their requirements?

Michael Hughes: Historically, companies have not needed granular (e.g., policy level) historical data for traditional products to support financial reporting needs. Granular data has generally been available for interest sensitive products in part due to FAS 97 reporting requirements.

Getting the granular data for traditional products has been a challenge, but the improved and more granular data management capabilities align with broader organisational objectives for many companies to support pricing, enforce management and customer and other management information needs.

LDTI is anticipated to introduce a lot of volatility on balance sheet. How concerning is this for actuaries and is it something that they have communicated to market?

Tara Wolf: The impact of LDTI on the income statement and balance sheet is a mixed bag. Bringing the liability for future policy benefits (LFPB) on to the balance sheet at current discount rates is intended to better match the accounting for the underlying assets so this should reduce balance sheet volatility. However, with assets and liabilities valued on a more consistent basis, asset-liability mismatches may become more transparent under LDTI.

Unlocking of LFPB assumptions will also increase volatility, but reflecting actual historical experience in the reserve valuation may reduce it. The prospective nature of DAC unlocking updates will also reduce volatility. The addition of more features in the market risk benefit (MRB) balance will likely introduce more volatility if these benefits/risks have not been included in hedging programs (consider variable annuity guaranteed minimum death benefits at many companies).

As each company's fact pattern and mix of business varies, these impacts will vary widely. As the impacts become clear, companies will begin to disclose and explain the impacts and help to educate financial statement users, but it will be a journey.

What are the challenges of interpreting results and communicating to the street?

Tara Wolf: Interpreting and communicating financial results over short periods of time for long duration products is inherently complicated. With GAAP LDTI, the challenges relate to the mixed nature of the accounting guidance, which often varies by product type or benefit feature, and the volatility considerations described above.

It also is driven by company fact patterns that vary widely, so it is hard to generalise and comparisons to peers will be a challenge. The enhanced disclosures will provide significant additional quantitative and qualitative information to investors on a quarterly basis, but I expect it will take some time for users of the financial statements to learn how to use and interpret the information. In some ways, learning a new accounting regime such as GAAP LDTI or IFRS 17 is like learning a new language. It will take some time to gain fluency. ■

A consultancy view

Valani Global reflects on the progress with insurers' implementation of LDTI.

Contributors:
Nazir Valani, President and Co-Founder, Valani Global
Sarah Valani, Co-Founder and Actuarial Consultant, Valani Global

How are you helping insurers with their LDTI implementation? What are the biggest challenges you are seeing with regards to this?

Insurers are seeking assistance with creating or refining models and processes with best practices in preparation for LDTI. They are encountering challenges using multiple actuarial, accounting and data software that do not seamlessly integrate with one another. LDTI has been a catalyst for insurers to consider enhancing their systems by moving towards end-to-end solutions that can better handle the increased data load, data grouping, new calculations and processes, increased detailed analysis and reporting requirements. With this strategic approach in mind, increased automation and controls within actuarial, accounting and data processes is top priority.

Beyond model and process changes, insurers have moved their focus from "what are we supposed to do?" to "what does this practically look like?". Understanding and explaining to stakeholders how assumption unlocking, future policy benefits, disaggregation of reserves, allocation of premium deficiency reserves, etc., affects how their business is reported is a complex task. Implementing a source of warnings analysis process is one way to assist insurers in understanding the drivers of change in business. This is especially important given that an increase in volatility of earnings is generally expected with the move to LDTI.

Are you finding the industry has enough granular data to meet their LDTI requirements? How can insurers access better quality data to meet the challenge?

The industry has a challenge with data and as a result we have seen that companies are choosing to implement a modified retrospective approach. The main questions insurers are encountering with data are:

- Is the required historical and output data available? Does the granularity of this data suffice under LDTI (e.g. experience analysis)? If the answer is no, simplifications will be required.
- How do we get new data requirements into

Nazir Valani, Valani Global

the model? Is it in the right format? This will require actuarial valuation areas to work with IT professionals to build long-term solutions.

Can you name some key systems challenges insurers might face with the new rules?

Data management, specifically historical data ETL [extract, transform, and load] processes, poses a large challenge for insurers. There has never before been such a large demand to compile detailed historical data or for data systems to serve as the single truth or baseline for actuarial, accounting and finance processes.

The increased demand for actuarial platforms has forced many insurers to switch to new actuarial software. It can be challenging to transfer knowledge within tight timelines and with limited project resources. As a result, insurers have asked consultants to assist employees with new actuarial platform functionality upskilling.

Integrating the subledger system with the actuarial software is also a challenge as it requires coordinated testing and transfer of data between different systems to populate new disclosures required for LDTI compliance.

To what extent have insurers needed to break down business silos to advance LDTI? Is this working?

To optimise compliance of LDTI, a strong partnership between actuarial, accounting, data, IT and finance teams is required. In preparation for LDTI, many insurers have formed a multidisciplinary management and project team comprising stakeholders from each business unit. Execution of a plan and timeline created with buy in from each unit has helped to break down business silos. Tasks frequently involve more than one business unit (e.g., connect data between actuarial and finance for the ledger and disclosures) as well as a high degree of automation.

The future demands for the integrated transformation of systems between actuarial, accounting, data, IT and finance teams is expected to only increase. With effective project management, insurers have created partnerships between these teams that will serve them well for years to come.

To what degree are you seeing insurers use LDTI as a catalyst for finance system modernisation?

Insurers are taking one of two approaches when faced with changes required for LDTI: minimum compliance or strategic improvements. Insurers taking the view that changes required to move towards compliance with LDTI are an opportunity for strategic improvements have undergone finance system modernisation efforts encompassing ledger/subledger, actuarial and data warehouse transformations.

What has influenced insurer choice of liability discount curve?

Guidance under LDTI prescribes insurers to discount using a single A rated bond yield curve:

- The standard says: "The liability for future policy benefits shall be discounted using an upper-medium grade (low credit-risk) fixed-income instrument yield."
- Moody's Investors Service defines a single A rated bond as follows: "Obligations rated A are judged to be upper-medium grade and are subject to low credit risk."

Sarah Valani, Valani Global

There can be some differences which result in a thick or fuzzy line for A rated bond yields, where the differences result from different credit risk within the A rating and different liquidity of the bonds with the same credit rating. Some insurers think it is appropriate to use slightly higher yielding A rated instruments that have less liquidity to discount liabilities that have less liquidity, but the standard does require the use of observable inputs, and it can be challenging to get the necessary observations for illiquid bonds.

The difference in the interest rate environment from issue to transition to LDTI will likely be a significant driver of reserve and balance sheet changes.

Has the industry got enough time to meet the effective date of 2023?

This implementation deadline is quickly approaching. A big push is required by SEC filers to meet the effective date of 2023 as insurers have been dealing with a lot of change in recent years, ranging from impacts of Covid-19 on their business, workforce and resources to change in regulation and transformation efforts. Leveraging lessons learnt from this initial group will be important for other insurers to meet the next effective date of 2025. ■